*Tension Between School Funds and Business Breaks*, WALL ST. J., July 18, 2001 at A1.

While Respondents generally agree with Petitioners about the great practical importance of the Sixth Circuit's ruling, Petitioners' concerns about the impact of the Sixth Circuit's decision on the ability of states to compete effectively for business investment and jobs are groundless. Indeed, econometric studies have repeatedly demonstrated that the actual influence of state and local tax incentives on business location decisions are, at most, marginal, both because of the small size of state and local taxes relative to other business costs and because competing jurisdictions all offer competing incentives. *See, e.g.*, Robert G. Lynch, RETHINKING GROWTH STRATEGIES (2004) 25-36; California Legislative Analyst's Office, *An Overview of California's Manufacturers' Investment Credit* 11 (Oct. 2002). As former Treasury Secretary and former Alcoa chief executive Paul O'Neill explains, "As a businessman I never made an investment decision based on the tax code . . . If you give money away I will take it, but good business people don't do things because of inducements." Joseph Kahn, *Treasury Choice Varies from Bush on Tax Outlook*, N.Y. TIMES, Jan. 18, 2001 at A-1, A-16.

Nor is there reason to fear, as Petitioners argue, that the Sixth Circuit's decision places the state of Ohio, or the other states in the Circuit, at a significant competitive disadvantage relative to other states. *See* State Pet. at 22-24; DaimlerChrysler Pet. at 10-11. Not only is there no evidence that investment tax credits like Ohio's are significant factors in business location decisions, but in any case, as Petitioners acknowledge, the decision below has cast a "cloud of uncertainty," *id.* at 9, over the comparable incentives offered by other states, and the incentives

offered by other states could only be influential "if businesses, *improbably*, disregard that uncertainty and rely on those incentives." *Id.* at 10 (emphasis added). Unsurprisingly, and notwithstanding the concerns raised in the State's Petition, Ohio's Governor continues to issue a steady stream of press releases touting new businesses and jobs that the state has been able to attract. *See, e.g.*, *Taft Applauds Federal Grant for Lima*, available at http://governor.ohio.gov/releases/072205Lima.htm (July 22, 2005) (discussing federal and state incentives used to secure ethanol production facility); *Taft Visits LORD Corporation to Celebrate Dayton Facility Expansion*, available at http://governor.ohio.gov/releases/072005LORD Corp.htm (July 20, 2005).

### B. The Sixth Circuit's finding that Ohio's ITC is unconstitutional follows directly from this Court's well-established Commerce Clause jurisprudence and should be affirmed.

The central concern of the Commerce Clause is "to avoid the tendencies toward economic Balkanization that had plagued the relations among the Colonies and later among the States under the Articles of Confederation." *Hughes v. Oklahoma*, 441 U.S. 322, 325-26 (1979).[1] Accordingly, this Court has long enforced an "anti-discrimination

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[1] *See also Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564, 571 (1997) ("to keep the commercial intercourse among the States free from all invidious and partial restraints") (quoting *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 231 (1824) (Johnson, J., concurring in judgment)); *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 328 (1977) ("the very purpose of the Commerce Clause was to create an area of free trade among the several states") (quoting *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327, 330 (1944)).

principle," *Maryland v. Louisiana*, 451 U.S. 725, 754 (1981), barring "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." *Oregon Waste Systems, Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 99 (1994). The Sixth Circuit's decision striking down Ohio's ITC is a straightforward application of this important and well-established principle.

As the Sixth Circuit explained, if an Ohio taxpayer locates a substantial new investment in plant and equipment within the state, it will benefit from a reduction in its Ohio franchise tax, whereas, if it locates the same investment elsewhere, it will continue to bear the full burden of Ohio taxation. *See* DaimlerChrysler Pet. App. at 6a. Thus, "as between two businesses, otherwise similarly situated and each subject to Ohio taxation, the business that chooses to expand its local presence will enjoy a reduced tax burden . . . while a competitor that invests out-of-state will face a comparatively higher tax burden. . . . " *Id.* This is, of course, precisely the end that the ITC is intended to achieve, favoring those businesses that choose to locate their facilities within the state and thereby also favoring the other in-state economic interests (employees, suppliers, etc.) who benefit from in-state facilities. And the ITC unquestionably achieves this end by discriminating in its treatment of otherwise identically situated business taxpayers, based solely on the in-state or out-of-state location of their investments.

Petitioners face a daunting task in attacking the Sixth Circuit's analysis. They are unable to point to a single case among this Court's numerous decisions applying the Commerce Clause's anti-discrimination principle in which the Court has upheld a measure that provided preferential

tax treatment conditioned upon in-state economic activity. In the absence of supportive case law, they instead seek to offer a restrictive reading of the Court's prior cases and discussions which will allow them to distinguish Ohio's ITC from the numerous provisions offering preferences for in-state activity which the Court has previously invalidated. The distinctions that they attempt to draw, however, can neither account for the full range of the Court's prior decisions, nor make sense of the Court's repeated explanations of its consistent prohibition against measures that "provid[e] a direct commercial advantage" to in-state business activity. *E.g., Maryland v. Louisiana*, 451 U.S. at 754; *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 329 (1977).

For example, Petitioners suggest that the Commerce Clause serves only to prohibit protectionist measures that shelter existing in-state interests from competition from interstate businesses, and not to reach measures which encourage out-of-state actors to direct their economic activity into the state. *See* DaimlerChrysler Pet. at 22-23; State Pet. at 20-21. But, while many of this Court's anti-discrimination cases have addressed such protectionist measures, the Court has never suggested the limitation asserted by Petitioners. On the contrary, the Court has repeatedly condemned measures as discriminatory precisely because they provided incentives for out-of-state businesses to locate their activities within the state. *See, e.g., Maryland v. Louisiana*, 451 U.S. at 756-57 (striking down credit because its "obvious economic effect . . . is to encourage natural gas owners . . . to invest in mineral exploration and development within Louisiana rather than invest in other States"); *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 72 (1963) (invalidating a measure

because it "encourages an out-of-state operator to become a resident in order to compete on equal terms"). As the Court has emphasized, "A State may no more use discriminatory taxes to assure that nonresidents direct their commerce . . . within the State than to assure that residents trade only in intrastate commerce." *Boston Stock Exchange*, 429 U.S. at 334-35.

In a similar vein, Petitioners contend that the Court's cases striking down state tax measures as discriminatory are confined to two clusters of situations – tariff-like measures that tax out-of-state goods or services, but not their in-state equivalents, and measures that penalize out-of-state activity by increasing taxes on the basis of such activity. *See* State Pet. at 19-20; DaimlerChrysler Pet. at 19, 22-24. Petitioners' suggestion is that a measure, like Ohio's ITC, which favors in-state activity by providing a selective benefit based on such activity, and not by imposing special burdens on out-of-state activity, does not run afoul of the Commerce Clause's anti-discrimination principle.

This bifurcated categorization of the case law had its origins in a 1986 law review article, written to contain the implications of the Court's rapidly expanding body of anti-discrimination tax cases, and particularly of the 1984 decision in *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984). *See* Philip Tatarowicz & Rebecca Mims-Velarde, *An Analytical Approach to State Tax Discrimination Under the Commerce Clause*, 39 VAND. L. REV. 879 (1986); *cf.* Robert J. Firestone, *State Investment Tax Credits Do Not Violate the Dormant Commerce Clause*, 36 STATE TAX NOTES 189 (2005) (applying the Tatarowicz/Mims-Velarde framework). But the Sixth Circuit was right, *see* DaimlerChrysler Pet. App. at 9a-10a, to reject

this attempted compartmentalization of the Court's anti-discrimination jurisprudence, because it can account neither for the Court's explanations of its reasoning nor for a number of its decisions. *See also* Walter Hellerstein & Dan T. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 CORNELL L. REV. 789, 813-15 (1996) (concluding that the Tatarowicz/Mims-Velarde framework fails to provide a satisfactory account of either the Court's reasoning or its decisions).

Petitioners' proposed framework depends on a crucial distinction between provisions that increase taxpayers' burdens due to out-of-state activity and those that merely diminish burdens on account of in-state activity. But Defendants are unable to cite a single case in which the Court has deployed such a distinction. On the contrary, the Court has expressly, and quite sensibly, disavowed any meaningful distinction, for anti-discrimination purposes, between tax benefits and burdens:

> Virtually every discriminatory statute allocates benefits or burdens unequally; each can be viewed as conferring a benefit on one party and a detriment on the other, in either an absolute or relative sense. The determination of constitutionality does not depend upon whether one focuses upon the benefited or the burdened party.

*Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 273 (1984).[2]

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[2] *See also Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 404 (1984) ("Nor is it relevant that New York discriminates . . . by disallowing a tax credit rather than by imposing a higher tax. The discriminatory economic effect of these two measures would be identical.")

Both Petitioners and Tatarowicz and Mims-Velarde themselves seek to deploy their analytic schema to limit the impact of the Court's holding in *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984), which found unconstitutional New York's corporate income tax credits that were measured by the extent of the taxpayer's export activities conducted in New York. As they emphasize, the *Westinghouse* Court observed that the scheme invalidated there, not only increased the credits as activity in New York increased, but also decreased the credits as activity elsewhere expanded, a feature that the Court described as the credit's "most pernicious feature." *Id.* at 401 n.9. But a thorough reading of the Court's opinion makes clear that this feature of the New York provision was not, as Petitioners insist, essential to the Court's ruling. In fact, the Court focused primarily on the benefits provided for New York activity, describing the provision as "an attempt to 'provide a positive incentive for increased business activity in New York.'" *Westinghouse*, 466 U.S. at 393. And when the Court offered three detailed examples of the workings of the credit, each intended to show the discriminatory effects of the provision, only the last of the three exemplified the "penalty" effect, while the other two focused instead on the benefits that result from increasing in-state activity. *Id.* at 401 n.9. As prominent scholars have observed, "The clear thrust of the opinion was that any provision that reduces the taxpayer's 'effective [in-state] tax rate' as the taxpayer engages in more in-state activity violates the Commerce Clause." Hellerstein & Coenen, *supra*, 81 CORNELL L. REV. at 815 (citations omitted). Even *Westinghouse* does not fit the Tatarowicz/Mims-Velarde framework.

Nor can their categorization accommodate a number of the Court's other anti-discrimination decisions. For example, in *Maryland v. Louisiana*, 451 U.S. 725 (1981), the Court struck down several aspects of Louisiana's tax on the transportation in Louisiana of off-shore natural gas, including a credit provision allowing taxpayers to use the tax on off-shore gas to reduce severance taxes on (unrelated) in-state mineral extraction. As the Court explained, the discriminatory feature of this provision was not any penalty imposed on out-of-state operations, but rather the benefit it provided for in-state activity and the resultant incentive "to invest in mineral exploration and development within Louisiana rather than invest in other States." *Id.* at 756-57. Other examples that cannot be accommodated within the Tatarowicz/Mims-Velarde framework include *American Trucking Ass'n, Inc. v. Scheiner*, 483 U.S. 266 (1987) (striking down Pennsylvania's flat-rate axle tax because it has the effect of favoring businesses using their trucks exclusively in-state) and *Camps Newfound/Owatonna v. Town of Harrison*, 520 U.S. 564 (1997) (invalidating a Maine property tax exemption restricted to charitable organizations providing the bulk of their services to in-state residents). The simple fact is that the Court's consistent approach has been to invalidate measures that are structured to favor in-state over out-of-state activity, without regard to whether the discrimination is achieved by providing a benefit for in-state activity or a burden on out-of-state alternatives.

Petitioners seek to reinforce their artificial narrowing of the Court's anti-discrimination case law by suggesting that, outside the narrow confines of their framework, the Court ordinarily endorses and approves state efforts to influence business location through tax policies. *See*

DaimlerChrysler Pet. at 16-18; State Pet. at 16. In fact, however, there is no body of Supreme Court case law upholding state tax measures on such grounds. On the contrary, in case after case, the Court has struck down tax provisions precisely because they attempt to steer business activities to a particular state. *See, e.g., Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 336 (1977) (holding that efforts to divert interstate commerce are "wholly inconsistent with the free trade purpose of the Commerce Clause"); *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 401 (1984) (noting that in "both *Maryland v. Louisiana* and *Boston Stock Exchange*, the Court struck down state tax statutes that encouraged the development of local industry"); *West Lynn Creamery v. Healy*, 512 U.S. 186, 193 (1994) (explaining the Commerce Clause as directed toward the avoidance of "distorting effects on the geography of production").

In the absence of supportive case law, Petitioners focus on scattered dicta that acknowledge the legitimacy of states acting to "encourage the growth and development of intrastate commerce and industry." DaimlerChrysler Pet. at 17 (quoting *Boston Stock Exchange*, 429 U.S. at 336-37). But these dicta offer nothing to support tax provisions that single out in-state economic activity for preferential treatment. On the contrary, they have consistently been careful to distinguish the legitimacy of the state's purposes from the acceptability of the means selected to further them, *see, e.g., Bacchus Imports*, 468 U.S. at 271, and to clarify that the permissible means do not include measures that discriminate in their treatment of in-state and out-of-state activity, *see, e.g., Boston Stock Exchange*, 429 U.S. at 329. The specific sorts of state competition for industry that the Court's dicta have countenanced, such as uniformly

applicable reductions of state taxes and government support for services needed by business, *see, e.g., West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 199 n.15 (1994), include only provisions that do not differentiate benefits or burdens based on a business's location.[3]

Finally, unable to find any support in the decisions of this Court, Petitioners contend that the Sixth Circuit's decision is in conflict with the ruling of the Michigan state courts in *Caterpillar, Inc. v. Department of Treasury*, 488 N.W.2d 182 (Mich. 1992). *See* State Pet. at 14-15; DaimlerChrysler Pet. at 11-12. But, as State Petitioners acknowledge, at 15, that case concerned a tax regime, and a tax benefit, dramatically different from those in the present case.

The tax involved in *Caterpillar* was Michigan's unique Single Business Tax, a form of value-added tax under which a business's tax liability is measured, not by its net income, but by its total business activity, including, *inter alia*, its costs for payroll and for acquisition of capital equipment, apportioned to reflect the portions of that activity attributable to Michigan. *See generally Trinova Corp. v. Michigan Dept. of Treasury*, 498 U.S. 358 (1991)

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[3] The State Petitioners go so far as to suggest that the *Westinghouse* Court specifically endorsed the use of tax incentives, including investment tax credits. *See* State Pet. at 16. But a full reading of the relevant passage, *Westinghouse*, 466 U.S. at 407 n.12, reveals that the Court was taking no position on this question, but was merely describing the position articulated by New York: "The Tax Commission seeks to classify the tax credit at issue here as an indirect subsidy to export commerce, similar to provision and maintenance of ports, airports, waterways, and highways; to provision of police and fire protection; and to enactment of job-incentive credits and investment-tax credits." The Court offers no opinion on which, if any, of such measures would pass constitutional muster.

(discussing Michigan's Single Business Tax). The challenged provision in *Caterpillar* was a "capital acquisition deduction" ("CAD") which adjusted the tax base to exclude the costs for capital acquisitions tied to Michigan business activity. Since the single business tax base was designed to include only the share of capital acquisitions attributable to its in-state activity, the Michigan court concluded that a deduction designed to be similarly restricted to capital acquisitions attributable to Michigan does not discriminate. "Since the tax base after apportionment represents only Michigan business activity, only capital acquisitions related to Michigan business activity should qualify for treatment pursuant to the CAD. The CAD . . . is designed to accomplish this result." *Caterpillar*, 488 N.W.2d at 186. In short, in the Michigan court's view, the CAD did not discriminate because both the tax base and the deduction were designed to include only those capital acquisitions attributable to Michigan, so that the CAD did not confer any competitive advantage on in-state capital investment. *See id.* at 192. Thus, in upholding the CAD, the Michigan court characterized both its purpose and its effects in ways entirely inapplicable to Ohio's ITC.

In sum, the Sixth Circuit's decision invalidating Ohio's ITC represents a straightforward application of a well established and central element of this Court's Commerce Clause jurisprudence. Despite Petitioners' claims, it raises no conflicts with the prior decisions of this Court, or of the lower courts, and, in fact, any contrary ruling would have required heroic efforts to distinguish and avoid this Court's numerous anti-discrimination precedents. Petitioners seek to cloud this fact by emphasizing the Court's observation in *Westinghouse* that its Commerce Clause analysis "has left much room for controversy and confusion

and little in the way of precise guides to the States in the exercise of their indispensable power of taxation." DaimlerChrysler Pet. at 13; State Pet. at 14 (quoting *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388, 403 (1984)). But, for the reasons explicated by the Sixth Circuit and in this Memorandum, just as the Court went on to observe in *Westinghouse*, "there is little room for such 'controversy and confusion' in the present litigation." *Id.*

## CONCLUSION

This case presents issues of great practical importance which would benefit from the Court's review. On the merits, the portion of the Sixth Circuit's decision invalidating Ohio's ITC follows straightforwardly from this Court's well-established Commerce Clause jurisprudence and should be affirmed.

Respectfully submitted,

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Supreme Court, U.S.
FILED
AUG 29 2005
OFFICE OF THE CLERK

(2)

No. 04-1724

**In The Supreme Court Of The United States**

WILLIAM W. WILKINS,
Tax Commissioner for the State of Ohio, et al.,
*Petitioners,*

v.

CHARLOTTE CUNO, et al.,
*Respondents.*

*ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT*

# REPLY BRIEF FOR THE PETITIONERS

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## TABLE OF CONTENTS

**Page**

TABLE OF CONTENTS ..... i

TABLE OF AUTHORITIES ..... ii

REPLY BRIEF FOR THE PETITIONERS ..... 1

A. Respondents concede that review is warranted as the Petition raises an important question of federal law on which clarity is urgently needed ..... 1

B. Respondents are wrong to assert that the decision below was a "straightforward application" of dormant Commerce Clause precedent ..... 4

CONCLUSION ..... 10

## TABLE OF AUTHORITIES

**Cases** **Page**

*American Trucking Ass'ns, Inc. v. Scheiner*,
483 U.S. 266 (1987) ..... 7

*Bacchus Imports, Ltd. v. Dais*,
486 U.S. 263 (1984) ..... 7, 8

*Boston Stock Exch. v. State Tax Comm'n*,
429 U.S. 318 (1977) ..... 7

*Camps Newfound/Owatonna, Inc. v. Town of Harrison*,
520 U.S. 564 (1997) ..... 8

*Caterpillar, Inc. v. Mich. Dep't of Treasury*,
488 N.W.2d 182 (Mich. 1992) ..... 4, 8

*Halliburton Oil Well Cementing Co. v. Reily*,
373 U.S. 64 (1963) ..... 7

*Maryland v. Louisiana*,
451 U.S. 725 (1981) ..... 6

*Westinghouse Elec. Co. v. Tully*,
466 U.S. 388 (1984) ..... 5, 6

**Additional Authorities** **Page**

P. Enrich, *Saving the State from Themselves: Commerce Clause Constraints on State Tax Incentives for Business*, 110 Harv. L. Rev. 377 (1996) ..... 4, 6

W. Hellerstein & D. Coenen, *Commerce Clause Restraints on State Business Development Incentives*, 81 Cornell L. Rev. 789 (1996) ..... 5

## REPLY BRIEF FOR THE PETITIONERS

### A. Respondents concede that review is warranted as the Petition raises an important question of federal law on which clarity is urgently needed.

Respondents agree with Ohio on the key issue currently before the Court: they concede that the Petition presents a question of vital importance that requires the Court's immediate attention. And in taking that position, Respondents are merely one voice in a chorus of remarkable depth and breadth. Twenty-seven States, along with a variety of labor unions, manufacturers and manufacturing associations, development agencies, tax foundations, chambers of commerce, and others have all filed amicus briefs supporting this Petition and/or Daimler-Chrysler's companion petition. See *DaimlerChrysler v. Cuno*, No. 04-1704. These briefs, authored from a wide range of perspectives, uniformly echo a common theme—the decision below threatens to disrupt accepted business development practices throughout the country, and, in doing so, will irreparably harm States and their citizens through lost development, lost opportunities, lost jobs and the loss in quality of life that will inevitably result.

As Respondents candidly concede, nothing about the decision below turns on any unique aspect of the Ohio Investment Tax Credit ("ITC"). Cuno Resp. Br. at 5. They admit that nothing about "Ohio's incentive programs is distinctively problematic." *Id.* Rather, Respondents level a broadside attack on *all* locational tax incentives, incentives that they acknowledge "virtually every state" employs. *Id.* at 1. Thus, by their own admission, this case involves not merely the hundreds of millions of dollars that DaimlerChrysler has invested in Toledo, nor only the tens of billions of dollars of Ohio-based investment that the incentive has spurred. Rather, the decision below affects hundreds of billions of dollars of existing and potential business investment across the country. And, as several amici

noted, given the international nature of capital markets, that investment could just as easily land overseas as here. See, e.g., Amicus Br. of Florida, 26 other States, and the District of Columbia at 6–7; Amicus Br. of Nat'l Governors Assoc. at 5–6; Amicus Br. of Nissan N. Am. at 9 (filed in No. 04-1704) ("The tax incentives offered to Nissan by Tennessee played a significant role in offsetting the very substantial wage differential between Tennessee and Mexico and thus were an important factor in Nissan's decision to invest in its [] Tennessee plant.").

Nor should anyone doubt that the decision below puts Ohio (and other Sixth Circuit States) at a competitive disadvantage as compared to its sister States in the interstate competition for new investment and new jobs. Respondents suggest that the impact of tax incentives is a most "marginal." See Cuno Resp. Br. at 7. This is so, they say, because business people rarely make their investment decisions based on the tax code. *Id.* Both common sense and common experience, however, belie those claims. It is difficult, if not impossible, to believe that a rational businessperson would *not* consider the tax implications of a proposed transaction. And amici provide plenty of examples showing that business people do in fact rely on such incentives. See, e.g., Amicus Br. of Mich. Mfg. Ass'n at 6–10 (filed in No. 04-1704) (providing examples of investments induced by tax incentives); Amicus Br. of Nissan N. Am. at 8–12 (filed in No. 04-1704) (describing impact of incentives); Amicus Br. of Ford Motor Co. and General Motors Corp. at 5 (filed in No. 04-1704) (same).

Moreover, the two studies Respondents cite in support of this "marginal" effect were conducted against a backdrop where all States were free to offer incentives. To be sure, it may be that where two or more States offer similar tax incentives for a given project, those incentives may largely "cancel out." But, if anything, that further illustrates the need for immediate review as the playing field is no longer level.

While the decision below undoubtedly casts a constitutional shadow over locational incentive programs throughout the country, it much more directly impacts such incentives in the Sixth Circuit. Thus, the decision hampers all States in their ability to compete with foreign countries, but also imposes a special harm on Sixth Circuit States in their competitive endeavors.

The breadth and ambiguity of the Sixth Circuit's language further underscores the need for review. As one amicus noted, to the extent that the decision below condemns all state action whose "economic effect" is to encourage investment in-state at the expense of development in other states, the decision could impact far more than state taxation. See Amicus Br. of Ky. Chamber of Commerce, et al. at 10. State spending on roads, railways, or even schools arguably has the "economic effect" of encouraging in-state development at the expense of out-of-state development. Alternatively, to the extent the decision imposes a "coercion" test or a "tax neutral decision making" test, it provides no meaningful limiting principle for such a test. As one amicus points out, "[n]early every business decision and investment involves tax consequences that are considered and influence the decision itself." Amicus Br. of Council on State Taxation, et al. at 11. In short, the broad terms of the decision create grave uncertainty regarding a whole range of state development activities, not merely state tax policy.

In light of the dramatic consequences of the decision below for business development activities throughout the nation, no one can seriously question (and indeed, no one does question) that the issue here qualifies as "an important question of federal law." S. Ct. Rule 10. State tax laws across the country are called into question, and only this Court can provide the needed clarity regarding what limits the dormant Commerce Clause imposes on locational incentives. Ohio joins Respondents and the overwhelming tide of amici in urging the Court to provide that clarity now.

**B. Respondents are wrong to assert that the decision below was a "straightforward application" of dormant Commerce Clause precedent.**

While it would be premature to focus on the merits of the dormant Commerce Clause claim, certain aspects of the merits arguments Respondents present in their acquiescence potentially impact the need for certiorari and accordingly warrant response here. First, Respondents are wrong to suggest that the decision below is merely a "straightforward application" of the Court's Commerce Clause jurisprudence. Cuno Resp. Br. at 9. In fact, as we noted previously, the better reading of the Court's precedent supports the constitutionality of the ITC. Ohio Cert. Pet. at 16–21. Second, Respondents are similarly incorrect in arguing that the decision here is consistent with the Michigan Supreme Court's decision in *Caterpillar, Inc. v. Michigan Department of Treasury*, 488 N.W.2d 182 (Mich. 1992). See Cuno Resp. Br. at 16–17.

1. The Court has never invalidated a franchise or income tax credit measured by, and limited to, a portion of new investment in the state. Thus, it is hard to see how a decision striking such incentives is a "straightforward application" of the Court's precedents. Indeed, academic commentators have expressly discussed the lack of certainty in the Court's jurisprudence on this issue. Respondents' counsel himself devoted a section of his 1996 article to attempting to refute "Some Doubts and Difficulties" with the theories that underlie Respondents' arguments here. P. Enrich, *Saving The States From Themselves: Commerce Clause Constraints On State Tax Incentives for Business*, 110 Harv. L. Rev. 377, 440–48 (1996).

With even greater candor, the very commentators upon whom the Sixth Circuit placed explicit reliance acknowledge that "income tax credits merely reward in-state activity by reducing the taxpayer's income tax bill and do not impose a

tax cost on out-of-state activity (aside from the opportunity cost of foregoing a reduction in in-state income tax liability)." W. Hellerstein & D. Coenen, *Commerce Clause Constraints on State Business Development Incentives*, 81 Cornell L. Rev. 789, 818 (1996). As a result, such credits would, they admit, "survive scrutiny under the penalty-based approach," which constitutes one way of reading the Court's precedents. *Id.* While of course favoring their own "state coercion" theory (and thereby rejecting the "penalty-based approach"), Hellerstein and Coenen admit they are advancing their theory in the context of "palpable tension in the Supreme Court's decisions," *id.* at 791, and against the background of an "ill-defined distinction between the constitutional carrot and the unconstitutional stick," *id.* at 792.

Respondents, in now disclaiming any such "palpable tension," make two key mistakes. First, in their discussion of *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984)—the only case they cite that involves credits against *income* taxes, such as the tax here—Respondents assert that the Court did not focus on whether the tax penalized out-of-state activity, but rather only on whether it benefited in-state activity. In particular, they assert that "the Court focused primarily on the benefits provided for New York activity, describing the provision as 'an attempt to "provide a positive incentive for increased business activity in New York."'" Cuno Resp. Br. at 13 (quoting *Westinghouse*, 466 U.S. at 393). This, they say, demonstrates that the Court does not take a penalty-based approach. *Id.* But, in fact, the Court looked beyond the benefits in invalidating the statute:

> Thus, not only does the New York tax scheme "provide a positive incentive for increased business activity in New York State," but also it ***penalizes increases in the [company's] shipping activities in other States***.

*Westinghouse*, 466 U.S. at 400–01 (emphasis added; citation omitted); see also P. Enrich, 110 Harv. L. Rev. at 445 (citing pages 400–01 of the *Westinghouse* opinion and recognizing that "the New York incentive imposed a direct penalty on out-of-state activity, and the Court emphasized this penalty as a particularly troubling feature of the provision"). *Westinghouse*, then, furnishes at least as much support for, as opposition to, a "penalty-based approach" to analyzing tax incentives. But, as Ohio noted in our Petition, under such an approach Ohio's ITC is unquestionably valid. See Ohio Cert. Pet. at 20–21. For purposes of the Petition, however, the key point is that, whatever one's final conclusion about the meaning of *Westinghouse*, the Sixth Circuit's apparent rejection of the "penalty-based approach" is not the "straightforward application" of *Westinghouse* that the Respondents suggest.

Respondents also place undue reliance on cases from the Court addressing tax provisions very different from the ITC in this case. Respondents contend that "the Court has repeatedly condemned measures as discriminatory precisely because they provided incentives for out-of-state businesses to locate their activities within the state," Cuno Resp. Br. at 10, but they rest that argument largely on *Maryland v. Louisiana*, 451 U.S. 725 (1981), and similar cases. The tax in *Maryland v. Louisiana*, however, is easily distinguishable. There, the Louisiana tax acted as a tariff on goods shipped through the state, but one that did not face manufacturers who also had offsetting activities within the state. 451 U.S. at 754–58. That is a far cry from the situation here, where Ohio imposes a tax not on out-of-state commodities, but on the conduct of business within the state, and where Ohio allows a credit against its tax that is both tied to, and limited by, a particular amount of new investment in the state. Ohio's ITC simply does not have the tariff-like effect that motivated the Court in *Maryland v. Louisiana*.

Nor do the other cases Respondents cite on this point offer any greater guidance. In *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), the Court found that Louisiana's use tax discriminated against interstate commerce by including certain costs in the tax base of equipment fabricated outside the state. Those same costs would not form part of the tax base if the equipment had been fabricated inside the state. *Id.* at 67–68. And *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318 (1977), addressed the tariff-like effect of a stock transfer tax that gave favorable treatment where the stock sale occurred in the state. *Id.* at 319. *Both* of those cases, however, involved imposition of additional tax burdens every time a particular business operation was performed outside the state. *Neither* addressed a tax break like Ohio's ITC that is measured by, and limited to, a portion of the specific amount of new investment in the state.

Additionally, Respondents are mistaken in their argument that the Court's other precedent conflicts with a "penalty-based approach." Cuno Resp. Br. at 14. In particular, *American Trucking Ass'ns, Inc. v. Scheiner*, 483 U.S. 266 (1987), is inapposite because it (1) did not involve any tax incentive and (2) did not involve a claim of facial discrimination. Instead, *Scheiner* found that a flat fee constituted de facto discrimination against trucks coming into the state because those trucks typically drove fewer miles in the state than the already-in-state trucks did. The unconstitutional result was that the flat fee had a higher per-mile impact on out-of-state trucks than on trucks based in the state. *Id.* at 281–87. Nothing about that holding addresses whether a tax credit can create an incentive to locate within a state as long as it does not penalize out-of-state activity. Nor does *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984), refute the "penalty-based approach" in a case like this one. *Bacchus* merely held invalid a tax preference intended to

benefit types of wine apparently produced only within the state. *Id.* at 265.

Finally, far from refuting the "penalty-based approach," *Camps Newfound/Owatonna v. Town of Harrison*, 520 U.S. 564 (1997), articulates a standard for facial discrimination that actually resembles that approach. Namely, "facial discrimination" is present where "the tax scheme functions by design and on its face to burden out-of-state-[interests] disproportionately." *Id.* at 579 n.13. The requirement that a provision not only impose some burden, but that it operate "by design" to impose a "disproportionate" burden, strongly parallels the penalty concept.

In short, the Court's cases are fully consistent with a penalty-based approach under which the dormant Commerce Clause simply prevents States from using their tax systems to penalize businesses for choosing to engage in out-of-state activities. And, as Ohio's Petition notes, such an approach is also consistent with the dormant Commerce Clause goals the Court has articulated. Ohio Cert. Pet. at 19–21. The Court might ultimately reject or confirm that approach, but it cannot fairly be said, as Respondents would have it, that "straightforward application" of Supreme Court precedent already compels adoption of their theory instead.

2. Nor are Respondents correct in minimizing the scope of the conflict between *Caterpillar, Inc. v. Michigan Department of Treasury*, 488 N.W.2d 182 (Mich. 1992), and the decision below. Cuno Resp. Br. at 16–17. To be sure, Respondents correctly point out that *Caterpillar* addressed the apportionment of Michigan's "capital acquisition deduction" ("CAD") rather than an ITC like Ohio's, and it is certainly true that the apportionment raised some constitutional concerns that the present case does not. But the Respondents' discussion simply ignores the two features of the Michigan decision that are plainly relevant here. First, Respondents fail to mention that the plaintiffs based their